NAMIBIA UNIVERSITY
OF SCIENCE AND TECHNOLOGY

FACULTY OF COMMERCE, HUMAN SCIENCES AND EDUCATION

DEPARTMENT OF ACCOUNTING, ECONOMICS & FINANCE

QUALIFICATION: BACHELOR OF ACCOUNTING (HONOURS)	
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COURSE CODE: AMA811S	COURSE NAME: ADVANCED MANAGEMENT ACCOUNTING
SESSION: JUNE 2022	PAPER: PRACTICAL AND THEORY
DURATION: 3 HOURS	MARKS: 100

FIRST OPPORTUNITY EXAMINATION QUESTION PAPER	
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INSTRUCTIONS

- This question paper is made up of FOUR (4) questions.
- Answer All the questions and in blue or black ink.
- Show all your working in the answer sheet.
- Start each question on a new page in your answer booklet and show all your workings.
- Questions relating to this paper may be raised in the initial 30 minutes after the start of the paper. Thereafter, candidates must use their initiative to deal with any perceived error or ambiguities and any assumption made by the candidate should be clearly stated.

PERMISSIBLE MATERIALS

Non-programmable calculator/financial calculator

THIS QUESTION PAPER CONSISTS OF 9 PAGES (Including this front page)

QUESTION 1 **[25 MARKS]**

MFP (Mutual Farm Products) was formed in 1910 as a co-operative shop network owned by farmers in the country of Azania. It progressively opened small shops across the country selling products produced by Azanian farmers. Over time its expanding network of shops began to offer non-farming products from a wide range of suppliers, but it has remained true to its co-operative roots. All employees are shareholders and receive annual dividends. Customers can also become shareholders and are rewarded with dividends which reflect the value of their spending in the shops. An increasing number of customers are becoming shareholders, reflecting a renewed interest in the country in mutual organisations, such as co-operatives. MFP only operates in Azania and it has no plans to expand overseas. Azania itself is a wealthy, industrialised country which continues to grow.

Supermarkets in Azania

When supermarkets were first introduced in Azania, MFP reflected this trend by opening its own supermarkets. However, its supermarkets tended to be (and continue to be) smaller than its well-known competitors and its network of smaller shops was largely retained. In contrast, other supermarkets focused on developing large out-of-town sites serving a large catchment population. In the top-ten supermarkets of Azania, only MFP has, in addition, a network of smaller shops.

In 2017 MFP was the eighth largest shop and supermarket chain in Azania. It reported revenues of N$10bn, compared to the N$40.5bn revenue of the market leader, HypCo. By 2021, MFP was the ninth largest shop and supermarket chain in the country, with revenues of N$11bn, compared with HypCo's N$45bn. During this period, two new supermarket chains have entered the Azanian market. These two new entrants, Super24/7 and Letto, already have a combined revenue of N$50bn and are fourth and eighth respectively in the top ten Azanian supermarket chains. Both of these companies are overseas-based supermarkets operating a no-frills approach to retailing. Overall, the revenue of the top ten supermarket chains has increased from N$300bn to N$350bn in the last five years.

Margins in the sector are always under pressure and the large supermarkets continue to aggressively market their goods, highlighting price savings. They also provide customer incentives, such as loyalty cards and account discount schemes in an attempt to retain customers. For many products and services, price comparison websites show consumers the prices charged by competing supermarkets.

With the exception of MFP, all supermarkets are quoted companies with their shares largely owned by institutional investors who look for significant dividends and capital appreciation. MFP is the only co-operative in the top ten Azanian supermarket chains. Generally, suppliers to supermarkets are relatively small companies. Supermarkets' control of consumer spending is so great that many suppliers aggressively compete to have their products stocked by the supermarket chains.

MFP has continued to promote and follow its ethical principles. It ensures that new shops and supermarkets are energy efficient. It also continues to pay its employees significantly more than its competitors. This concern for its employees' welfare appears to lead to excellent customer service performance. For example, in a recent independent survey of supermarket customers, MFP was ranked first for personal customer service.

There is some evidence that people in Azania are becoming disillusioned with their supermarkets and this is reflected in **Appendix A**, an extract from an article by the journalist Liz Bones in the influential daily newspaper, Arbor Today. Appendix B is an extract from an information sheet issued by the government to companies trading in Azania.

Management at MFP

Management at MFP is aware that the company has certain weaknesses. For example, it acknowledges that it needs to streamline its supply chain and achieve cost savings. It also recognises that it has failed to exploit technological advances in product control, movement and storage.

However, before making changes, the management wishes to better understand the strategic position of MFP and the models used to assess this position. It has asked for a report which includes:

– An explanation of the purpose and value of PESTEL analysis and Porter's five forces framework.

– An analysis which identifies external factors from the perspective of four elements of the PESTEL analysis: political, sociocultural, environmental and legal.

– An analysis of the market place using Porter's five forces framework.

– The potential role of critical success factors (CSFs), key performance indicators (KPIs) and integrated reporting on formulating and monitoring strategy at MFP. The company does not currently use such concepts.

Appendix A: Have Azanians fallen out of love with the supermarket? By Liz Bones

For many years, the trend towards supermarket shopping has seemed unstoppable. The high streets of our towns have become increasingly deserted as grocers, butchers, toy shops and bookshops have disappeared under the combined onslaught of online retailers and expanding supermarkets. For example, ten years ago in the high street of Milton Magna there were three grocers, four butchers, two toy shops, one bookshop and only two supermarkets. Now, only one grocer and one butcher survive on the high street and both supermarkets have moved to out-of-town locations. In fact there are now five out-of-town supermarkets serving the people of Milton Magna.

However, there is increased evidence that shoppers are becoming disillusioned with supermarkets and yearn to return to the days when shops were smaller and service more personal.

Fiona McLean, of the department of sociology MidShire University, says that, 'our research suggests that there is a significant number of consumers, commonly called green consumers, who are increasingly concerned about the environmental impact of food and other products that they are purchasing. This is not only in terms of the excessive and elaborate packaging of the goods, but also in terms of the 'food miles' that the product has travelled before it reaches the shelves of the shop or supermarket.'

In general, these green consumers have higher than average disposable income and they are prepared to pay a price premium for products which have been ethically sourced. Fiona also suggested that such consumers are part of a group who are increasingly angered by what they consider as the excessive profits of the large supermarket chains, the high remuneration packages paid to senior management and the large dividends paid to their institutional shareholders. 'There is a feeling that supermarkets are run by fat-cat managers, exploiting small suppliers to reduce costs to create a margin for dividends that pacify demanding institutional investors', she said.

Even the newer entrants, Super24/7 and Letto, are under threat. There is a consumer reaction against these overseas-based supermarkets which have followed a low-cost, no frills approach, with shelves stacked intensively with low priced products and where customer service is both impersonal and kept to a minimum. The low wages paid to staff in these supermarkets is also an issue for the green consumer.

So, perhaps Azania is on the brink of a supermarket revolution! Television personalities such as Alexis Piazzio urge us to 'think local' and 'shop local'. Perhaps after all, small is beautiful when it comes to shopping!!!

Appendix B: Azanian government information sheet 4560 (extract)

Disability legislation (The Access Act)

The recent extension of disability access legislation requires shops and supermarkets to help all disabled customers to access all shelf areas within the store. The previous legislation just required shops and supermarkets to provide disability access to the store areas. However, many disabled customers found that goods were out of reach when they were actually in the store. This extension to the legislation addresses this issue. So, for example, all products held within the store must be reachable for a person who is in a wheelchair and, if not, a store attendant must help. Failure to adhere to this legislation will lead to a fine of up to N$1,000 per incident.

Pension reform

The new government recognises that the current state funded schemes will lead to a significant pension shortfall in the future. Consequently, it has declared its intentions to make it mandatory for employees to pay 5% of their gross pay into a pension scheme of their choice. The amount paid in will be matched by that paid in by the employer. So, for example, an employee earning N$10,000 per year will pay N$500 per year into his or her pension fund and the employer will also be required to pay N$500 per year into the same fund. It proposes that the employer will be responsible for ensuring that pension payments are correctly made into government authorised schemes and to accurately process these payments, through automatic payroll deductions, every month. These proposals for pension reform are currently under discussion.

Required:

Write the report required by MFP management which:

(a) Analyses external factors from the perspective of FOUR elements of the PESTEL analysis: political, sociocultural, environmental and legal. The analysis should include an assessment of the likely effect of such factors in the context of the strengths and weaknesses of MFP. It should also include an explanation of the purpose and value of a PESTEL analysis. **(13 marks)**

(b) Analyses the market place (industry) using Porter's five forces framework, assessing its implications for MFP.This analysis should also include an explanation of the purpose and value of the five forces framework. **(12 marks)**

QUESTION 2 [25 MARKS]

The directors of Kairaratjo Co are considering a planned investment project costing N$25m, payable at the start of the first year of operation. The following information relates to the investment project:

	Year 1	Year 2	Year 3	Year 4
Sales volume (units/year)	520,000	624,000	717,000	788,000
Selling price (N$/unit)	30·00	30·00	30·00	30·00
Variable costs (N$/unit)	10·00	10·20	10·61	10·93
Fixed costs (N$/year)	700,000	735,000	779,000	841,000

This information needs adjusting to take account of selling price inflation of 4% per year and variable cost inflation of 3% per year. The fixed costs, which are incremental and related to the investment project, are in nominal terms. The year 4 sales volume is expected to continue for the foreseeable future.

Kairaratjo Co pays corporation tax of 30% one year in arrears. The company can claim tax-allowable depreciation on a 25% reducing balance basis.

The views of the directors of Kairaratjo Co are that all investment projects must be evaluated over four years of operations, with an assumed terminal value at the end of the fourth year of 5% of the initial investment cost. Both net present value and discounted payback must be used, with a maximum discounted payback period of two years. The real after-tax cost of capital of Kairaratjo Co is 7% and its nominal after-tax cost of capital is 12%.

Required:

(a) (i) Calculate the net present value of the planned investment project. **(12 marks)**

(ii) Calculate the discounted payback period of the planned investment project. **(4 marks)**

(b) Discuss the financial acceptability of the investment project. **(3 marks)**

(c) Critically discuss the views of the directors on Kairaratjo Co's investment appraisal. **(6 marks)**

QUESTION 3 [25 MARKS]

The following statement of financial position information relates to Tara Ltd, a company listed on a large stock market which pays corporation tax at a rate of 30%.

	N$m	N$m
Equity and liabilities		
Share capital	17	
Retained earnings	15	
	——	
Total equity		32
Non-current liabilities		
Long-term borrowings	13	
Current liabilities	21	
	——	
Total liabilities		34
		——
Total equity and liabilities		66
		——

The share capital of Tara Ltd consists of N$12m of ordinary shares and N$5m of irredeemable preference shares.

The ordinary shares of Tara Ltd have a nominal value of N$0·50 per share, an ex dividend market price of N$7·07 per share and a cum dividend market price of N$7·52 per share. The dividend for 2022 will be paid in the near future. Dividends paid in recent years have been as follows:

Year	2021	2020	2019	2018
Dividend (N$/share)	0·43	0·41	0·39	0·37

The 5% preference shares of Tara Ltd have a nominal value of N$0·50 per share and an ex dividend market price of N$0·31 per share.

The long-term borrowings of Tara Ltd consist of N$10m of loan notes and a N$3m bank loan. The bank loan has a variable interest rate.

The 7% loan notes have a nominal value of N$100 per loan note and a market price of N$102·34 per loan note. Annual interest has just been paid and the loan notes are redeemable in four years' time at a 5% premium to nominal value.

Required:

(a) Calculate the after-tax weighted average cost of capital of Tara Ltd on a market value basis. **(15 marks)**

(b) Discuss the circumstances under which it is appropriate to use the current WACC of Tara Ltd in appraising an investment project. **(5 marks)**

(c) Discuss THREE advantages to Tara Ltd of using convertible loan notes as a source of long-term finance. **(5 marks)**

QUESTION 4 [25 MARKS]

Dongo Ltd is an international airline which flies to destinations all over the world. Dongo Ltd experienced strong initial growth but in recent periods the company has been criticised for under-investing in its non-current assets.

Extracts from Dongo Ltd's financial statements are provided below.

Statements of financial position as at 30 April:

	2022	2021
	N$'000	**N$'000**
Assets		
Non-current assets		
Property, plant and equipment	317,000	174,000
Intangible assets (note ii)	20,000	16,000
	337,000	190,000

Current assets		
Inventories	580	490
Trade and other receivables	6,100	6,300
Cash and cash equivalents	9,300	22,100
Total current assets	15,980	28,890
Total assets	**352,980**	**218,890**
Equity and liabilities		
Equity		
Equity shares	3,000	3,000
Retained earnings	44,100	41,800
Revaluation surplus	145,000	Nil
Total equity	**192,100**	**44,800**
Liabilities		
Non-current liabilities		
6% loan notes	130,960	150,400
Current liabilities		
Trade and other payables	10,480	4,250
6% loan notes	19,440	19,440
Total current liabilities	**29,920**	**23,690**
Total equity and liabilities	**352,980**	**218,890**

Other EXTRACTS from Dongo Ltd's financial statements for the years ended 30 April:

	2022	**2021**
	N$'000	**N$'000**
Revenue	154,000	159,000
Profit from operations	12,300	18,600

Finance costs	(9,200)	(10,200)
Cash generated from operations	18,480	24,310

The following information is also relevant:

(i) Dongo Ltd had exactly the same flight schedule in 2022 as in 2021, with the overall number of flights and destinations being the same in both years.

(ii) In January 2022, Dongo Ltd had to renegotiate its licences with five major airports, which led to an increase in the prices Dongo Ltd had to pay for the right to operate flights there. The licences with ten more major airports are due to expire in December 2022, and Dongo Ltd is currently in negotiation with these airports.

Required:

(a) Calculate the following ratios for the years ended 30 April 2021 and 2022:

(i) Operating profit margin;

(ii) Return on capital employed;

(iii) Net asset turnover;

(iv) Current ratio;

(v) Interest cover;

(vi) Gearing (Debt/Equity).

Note: For calculation purposes, all loan notes should be treated as debt. **(12 marks)**

(b) Comment on the performance and position of Dongo Ltd for the year ended 30 April 2022.

Note: Your answer should highlight any issues which Dongo Ltd should be considering in the near future. **(13 marks)**

THE END